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1965

MERCANTILE STORES COMPANY, INC.

AND SUBSIDIARIES

Annual Report

FOR THE YEAR ENDED JANUARY 31, 1966

MERCANTILE STORES COMPANY, INC.

LIST OF OUR STORES

BACON'S (Estab. 1845)
  Louisville, Ky.
    St. Matthew's
    Shively
    Jeffersonville, Ind.

CASTNER-KNOTT (Estab. 1898)
  Nashville, Tenn.
    Green Hills
    Donelson
    Shelbyville
    Harding Mall
      (Opened March, 1966)

CREWS-BEGGS (Estab. 1888)
  Pueblo, Colo.

O. J. De LENDRECIES (Estab. 1879)
  Fargo, North Dakota

GAYFER'S (Estab. 1879)
  Mobile, Ala.
    Springdale
    Pensacola, Fla.
    Edgewater, Miss.

GLASS BLOCK (Estab. 1887)
  Duluth, Minn.

HENNESSY'S (Estab. 1885)
  Butte, Mont.
    Helena

JONES (Estab. 1887)
  Kansas City, Mo.
    Blue Ridge
    Troost Ave.
    Independence
    Prairie Village, Kans.
    Pittsburg, Kans.
    Muskogee, Okla.

JOSLIN'S (Estab. 1873)
  Denver, Colo.
    Englewood
    Lakewood
    Greeley
    Merchants Park
    Boulder
    Aurora
    Villa Italia
      (Opened March, 1966)

LAZARUS (Estab. 1889)
  Wilkes-Barre, Pa.

LION (Estab. 1857)
  Toledo, Ohio
    Westgate

McALPIN'S (Estab. 1852)
  Cincinnati, Ohio
    Kenwood
    Western Hills
    Cherry Grove
    Middletown

MONTGOMERY FAIR (Estab. 1868)
  Montgomery, Ala.
    Eastbrook
    Opelika

PEOPLES (Estab. 1888)
  Tacoma, Wash.
    Yakima
    Lakewood
    Port Angeles
    Wenatchee
    Olympia (Lacey)
      (To Open May, 1966)

THE RIGHT HOUSE (Estab. 1843)
  Hamilton, Ontario, Canada
    Brantford
    Galt
    St. Catharines

ROOT'S (Estab. 1856)
  Terre Haute, Ind.
    Sullivan
    Robinson, Ill.

J. B. WHITE (Estab. 1874)
  Augusta, Ga.
    National Hills
    Aiken, S. C.

J. B. WHITE (Estab. 1874)
  Columbia, S. C.—Richland Mall

•

Represented in the markets by
MERCANTILE STORES COMPANY, INC. (N. Y.)
(A wholly owned subsidiary company)
128 W. 31st Street, New York, N. Y.
Cable Address: *Merstore*

MERCANTILE STORES COMPANY, INC.

BOARD OF DIRECTORS

JOHN E. BIERWIRTH
F. K. BRADLEY
MORGAN A. CASEY
ASHTON HAWKINS
HAROLD W. JOCKERS
F. G. KINGSLEY
GERRISH H. MILLIKEN, JR.
MINOT K. MILLIKEN
ROGER MILLIKEN
GEORGE S. MOORE
R. NELSON SHAW
RALPH S. STILLMAN

OFFICERS

HAROLD W. JOCKERS, *Chairman of the Board*
R. NELSON SHAW, *President*
F. G. KINGSLEY, *Chairman of the Executive Committee*
F. K. BRADLEY, *Vice-Chairman of the Board*
MORGAN A. CASEY, *Vice-President & Treasurer*
CHARLES E. STALLINGS, *Vice-President*
FREDERICK W. BLECKWENN, *Vice-President*
EDWARD J. SHARKEY, *Vice-President*
R. S. KIZER, *Controller*
ASHTON HAWKINS, *Secretary*

Stock Transfer Agent
CHEMICAL BANK NEW YORK TRUST COMPANY
20 Pine Street
New York

Registrar of Stock
FIRST NATIONAL CITY BANK
399 Park Avenue
New York

FINANCIAL HIGHLIGHTS

IN BRIEF

	1965 (Year ended Jan. 31, 1966)	*1964* (Year ended Jan. 31, 1965)
Sales	$220,610,170	$207,260,905
Sales Increase Percentage	6.4%	7.7%
Profit Before Income Taxes	16,590,344	14,252,235
Percent to Sales	7.5%	6.9%
Net Profit	8,600,344	7,132,235
Profit Per Share	$2.92	$2.42
Dividends Paid:		
Per Share	$1.20	$1.20
Percentage of Profit Paid Out	41%	50%
Cash Flow:		
Amount in Dollars	11,956,000	10,572,000
Amount Per Share	$4.06	$3.59
Book Value Per Share	$22.82	$21.45
Working Capital	42,075,189	39,567,014
Ratio of Net Profit to Invested Capital	12.8%	11.3%

MERCANTILE STORES COMPANY, INC.

AND SUBSIDIARIES

100 West 10th Street
Wilmington, Delaware
April 15, 1966

Fellow Stockholders:

This is the annual report for the year ended January 31, 1966, our forty-seventh year. The Company again made new record highs in sales and profits.

Sales amounted to $220,610,170. Net profit for the year was $8,600,344. Earnings per share amounted to $2.92.

Profit

Business activity in general continued at a high level during 1965, and our Company shared in the prosperity of the country. Our profit for the year was the highest in the history of the Company by a considerable margin. The pretax profit of $16,590,344 was $2,338,109 higher than last year's figure of $14,252,235. (Last year was the record high at that time.) The net profit of $8,600,344 was better than last year by $1,468,109.

The percentage of pre-tax profit to sales showed a gain over last year of .6%—from 6.9% to 7.5%. This percentage has shown steady improvement over the past four years as shown below:

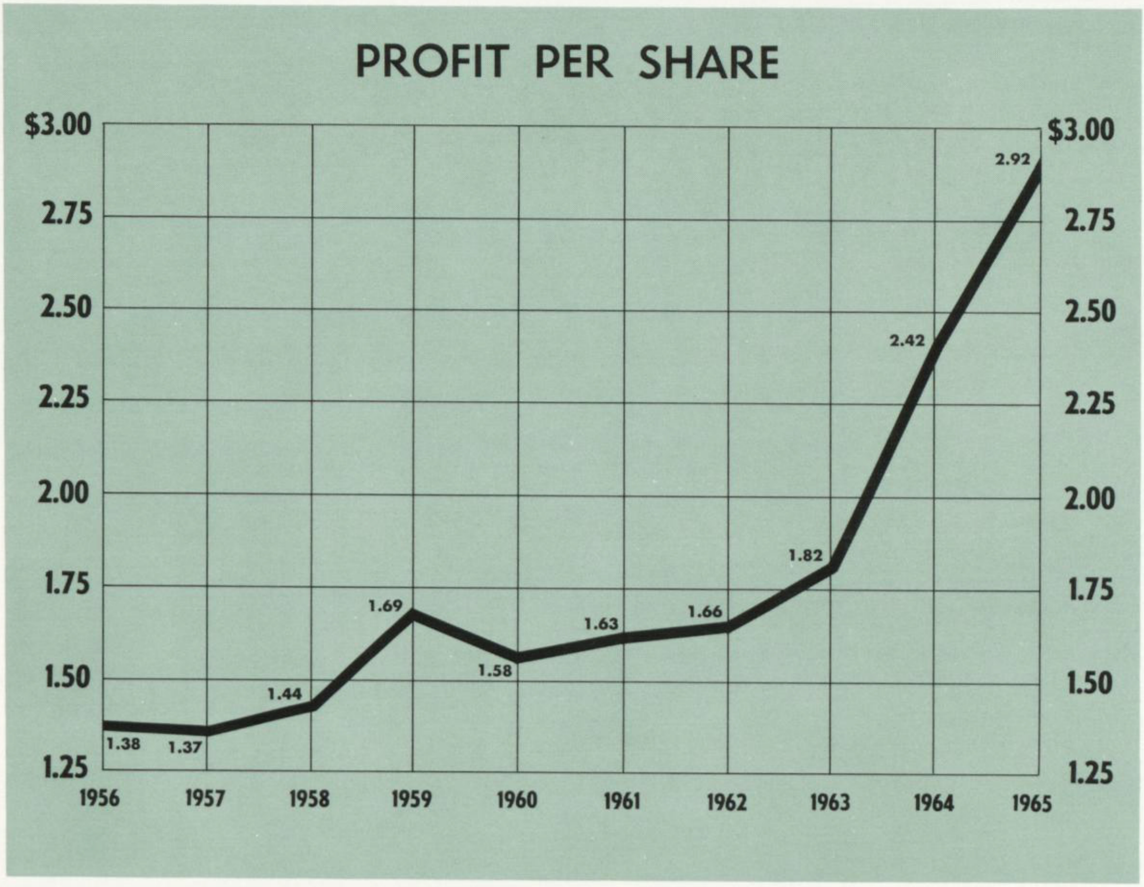
Year Ended	
January 31, 1963	5.6%
January 31, 1964	5.8%
January 31, 1965	6.9%
January 31, 1966	7.5%

The sales increase of $13,349,265 was the most important factor in the profit increase. A slight increase in mark-downs was more than offset by an improvement in mark-up. In expense control, the results were good. The expense percentage to sales was reduced from last year. This is the second consecutive year that this percentage has dropped. Prior to these latest two years there was a period of several years during which the expense ratio was creeping up steadily, despite management's efforts to halt the increase. The expense ratio for the year just closed was the lowest since 1957.

The comparison of profits of last year and this year was not distorted by any significant unusual factor, other than the reduction in Federal income tax rates which improved the profit for this year by about 10 cents per share.

The profit per share of $2.92 is a record high for our Company. Last year's figure of $2.42 was the previous high. The earnings per share increased 50 cents, an increase of 21%.

The chart on the opposite page gives the profit per share for the last ten years. As the chart shows, the profit per share of $2.92 is more than double the profit per share of ten years ago.



Sales

The sales total for the year was $220,610,170. This is the eleventh year in a row in which a new sales record has been set. The sales increase amounted to $13,349,265 equivalent to 6.4%. The opening of new units was not the cause of this increase. Sales in comparable stores which were open for the full twelve months in both years, showed an increase of 6.6%.

For the first time, our business in suburban stores in the year just closed, amounted to more than half of our total sales—with 53% from these newer stores and 47% from the older downtown stores. The proportion of our business in suburban stores will be still larger in the year just started. This points to an important change in the character of our business which has developed in recent years. As recently as 1950, our sales in suburban stores amounted to only 15% of total Company sales. Since 1950 the proportion of our business done in suburbs has increased each year.

A review of the latest ten years shows a substantial growth in our Company, summarized as follows:

> Total Company sales increased from $138,785,704 to $220,610,170, an increase of $81,824,466 or 59%.
>
> Seventeen new stores were added, which contain 1,426,000 square feet of space. (During the same period fourteen stores—mostly small stores—were closed representing 271,000 square feet of space.)

Geographically, about 80% of our business comes from the middle western and southern part of the United States. The table below shows the breakdown of our latest year sales into four regional divisions:

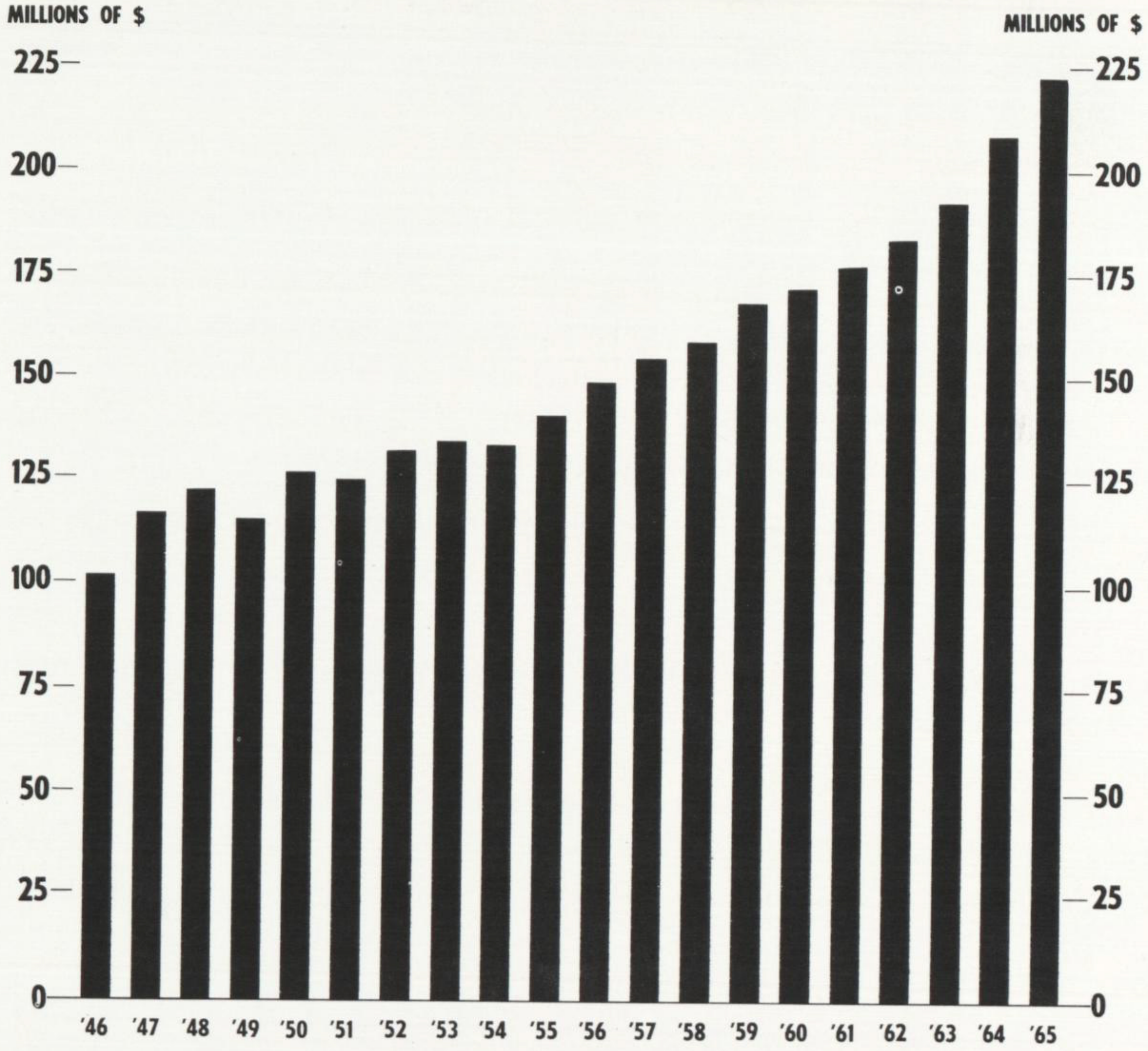
Southern stores	34%
Middle western stores	46%
Western stores	14%
Eastern and Canadian stores	6%
	100%

The chart opposite shows the total sales of the Company for the last twenty years. Since 1939 there have only been three years in which sales did not go ahead. The last year we had a sales decrease was 1954.

Inventory

Merchandise inventories (including goods in transit) amounted to $32,178,978 at January 31, 1966. This was higher than a year ago by $2,054,684, an increase of 6.8%. The percentage increase in inventories (6.8%) was very close to the sales increase for the year (6.4%).

SALES DURING PAST 20 YEARS



Square Feet of Store Properties

At January 31, 1966 there were approximately 4,427,000 square feet of space in our store properties. During the year just started, we expect to add about 335,000 square feet to the Company total. The additional space will come from new stores and from relocating and expanding existing stores (details are given under "Expansion").

The figures of square footage given above, represent the total space in our store buildings. Part of the space in store buildings is necessarily used for stockrooms, offices and other "non-selling" functions. Separate warehouse properties are not included in the figures given.

Dividends

Dividends were paid during this past year at the rate of $1.20 per share. The dividend rate has been increased. The new rate is 20 cents per year higher which brings the annual rate to $1.40. The Board of Directors announced in December, 1965, its intention to place the stock on a $1.40 basis for the coming year. The first quarterly dividend of 1966 (March 15) has been paid at the higher rate of 35 cents—the former quarterly rate was 30 cents.

During the year just closed, four quarterly dividend payments of 30 cents each were made on March 15th, June 15th, September 15th and December 15th. The total dividends paid during 1965 amounted to $3,537,382 which was the same as the year before.

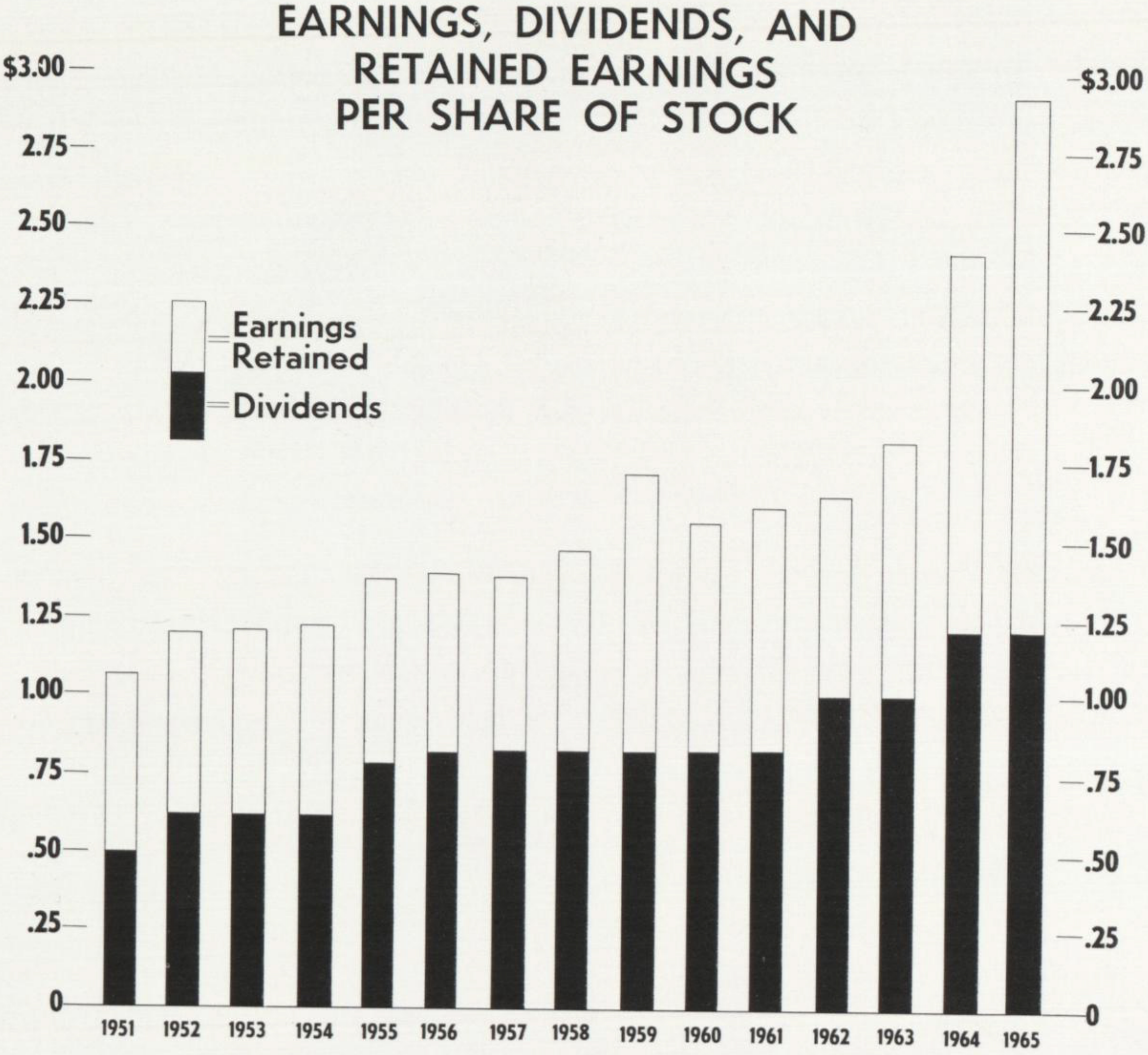
The dividend rate for four years is shown below:

Calendar Year	Dividend Rate Per Share
1966	$1.40
1965	1.20
1964	1.20
1963	1.00

The dividends paid during 1965 were equal to about 41% of the net profit for the year. For the past ten years, the dividend pay-out has averaged about 52%—net profit for the ten years totaled about $52,694,083 and the dividends paid during those ten years totaled about $27,487,383. The Company has paid dividends for the past twenty-six years without interruption, and the dividend has never been reduced during that time.

There were 5,772 stockholders in our Company at January 31, 1966.

A comparison of net profit, dividends paid and retained earnings during the last fifteen years is shown in the chart on the opposite page. The amounts are expressed in dollars per share.



Expansion During the Year Under Review

The principal changes in our store properties during the year ended January 31, 1966 were as follows:

Additions:

One new store opened

One major store completely remodernized and enlarged

Relocation:

One major downtown store relocated to the suburbs

Closings:

One major downtown store closed

Four small appliance stores closed

One small junior store closed

Details of Additions:

In March, 1965, we opened an attractive store in Helena, Montana which is the capital city of that state. The new store of about 44,000 square feet is operating under the Hennessy name as a branch of our Hennessy store in Butte, Montana. The Hennessy store in Butte is the leading store in that city. The store opened in Butte in 1885.

Our Joslin store in downtown Denver, Colorado was completely modernized and enlarged during 1965 at a cost in excess of two million dollars. About 32,000 square feet of space was added. The new plant was completed in June, 1965.

Relocation:

In February, 1965, we closed our downtown Montgomery Fair store in Montgomery, Alabama, and eight days later opened a beautiful new store in the suburbs of Montgomery. The old store contained about 140,000 square feet. The new store has about 167,000 square feet (about 123,000 square feet are in use now with the balance reserved for expansion). We now operate three Montgomery Fair stores—two in suburban Montgomery and one in Opelika, Alabama, which is about sixty miles from Montgomery.

Stores Closed:

We closed the MacDougall & Southwick store in downtown Seattle, Washington in January, 1966. The lease on the property expired and we were able to terminate the operation at a minimum cost. This store of 103,000 square feet was one of the original stores acquired when the Company was formed in 1919. In recent years it has been a marginal operation. The store fell short of earning a satisfactory return on its invested capital and we closed it. It is Company policy to measure each store's operation by the return that store makes on the capital invested in the store.

The four small appliance stores which were operated as branches of MacDougall & Southwick, were also closed.

We closed a small junior store in Paris, Illinois in June, 1965.

The combined sales of the stores closed (MacDougall's, 4 appliance stores and Paris) amounted to about $4,000,000 during the year ended January 31, 1966.

Current Number of Stores:

The stores currently in operation are listed in the front of this report (with notations of stores to open later in 1966). At January 31, 1966 the stores operating consisted of 18 major department stores and 40 branches.

Expansion During Calendar Year 1966

During the calendar year 1966 our business will be substantially expanded in seven locations, summarized as follows:

Three new stores will be opened

Two existing stores will be enlarged substantially

Two stores will be relocated in larger quarters

The three new stores will add 190,000 square feet of space, the enlarging of two stores will add 100,000 square feet, and the two relocations will add 45,000 square feet—making a total of 335,000 square feet to be added to the Company total at January 31, 1966 of 4,427,000 square feet. This will be an increase of about 7.6% in space.

After a year or two we would estimate this expansion will add about $16,000,000 to the annual sales of the Company. A rough estimate of the amount of added sales from this expansion which will go into sales of the year just started, is between $5,000,000 and $7,000,000.

Regarding the three new stores to be opened—one is in suburban Denver, Colorado, one in suburban Nashville, Tennessee and the third is in the Olympia region outside of Tacoma, Washington.

As to the two existing stores to be enlarged, one is in suburban Mobile, Alabama and the other is in suburban Cincinnati, Ohio.

Regarding the relocations to larger quarters—one store is in Yakima, Washington and the other in Aiken, South Carolina.

* * * *

On the next two pages are pictures of our beautiful newly modernized Joslin store in downtown Denver, Colorado and the fine new Montgomery Fair store in suburban Montgomery, Alabama.

MONTGOMERY
Fair

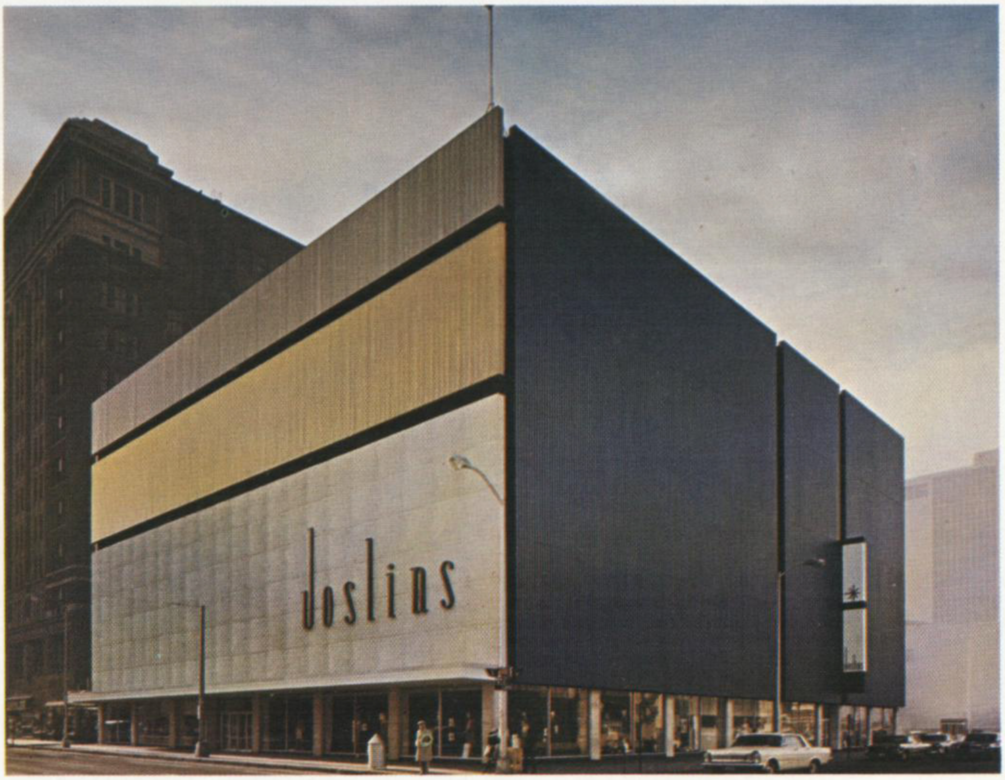
ABOVE — *Exterior of our new store in Montgomery, Alabama.*

BELOW — *Part of the fashion floor in our modernized Denver, Colorado store.*

Russell Stover
Greeting Cards

ABOVE — *View of main floor in new Montgomery store.*

BELOW — *Exterior of Denver store.*



Additions and Improvements to Physical Properties

The Company invested $4,560,238 in land, buildings and fixtures during the year just closed. For the past ten years comparable expenditures for capital assets have averaged about $5,215,152 per year. It is difficult to predict the completion date of some of the planned projects, but present indications point to a total of between $5,500,000 and $6,500,000 for capital asset expenditures during the year we are now in.

The following is a summary of the expenditures for the year ended January 31, 1966:

For new stores	$1,373,043
For relocating stores to larger quarters	662,022
For enlarging and modernizing stores	1,277,215
For keeping existing properties in good condition	1,247,958
Total	$4,560,238

The largest amount spent in any one location was $700,826 expended in Denver. This completed the modernization of our downtown Joslin Store at a total cost of a little over two million dollars.

Depreciation charged to operations for the year under review was $3,243,417. This was $169,872 less than the preceding year. Quite apart from the capital expenditures and depreciation, the Company spent $730,689 for repairs and maintenance, which was charged to operations.

Where the Funds Have Come From for the Expansion

The Company has invested $52,151,523 in its properties for new stores and improvements during the last ten years, as follows:

Year Ended	Capital Expenditures
January 31, 1957	$ 9,876,679
January 31, 1958	6,440,533
January 31, 1959	5,945,457
January 31, 1960	4,618,077
January 31, 1961	3,743,852
January 31, 1962	4,167,115
January 31, 1963	4,883,272
January 31, 1964	4,145,524
January 31, 1965	3,770,776
January 31, 1966	4,560,238
	$52,151,523

Nearly three quarters of the funds have come from retained earnings, with the remainder from long term borrowings and sale lease-back arrangements, as follows:

From retained earnings	$38,373,401
From increase in long term debt (ten years ago long term debt was $5,562,865 and currently it is $15,857,693—increase in ten years was $10,294,828)	10,294,828
Proceeds from three sale lease-back arrangements	3,483,294
	$52,151,523

Use of Electronic Data Processing

Further progress was made during the year in applying electronic data processing methods to our business. Because many of our stores are widely separated across the country, we are setting up regional computer centers at strategic points in various parts of the country. Under this system, data is transmitted over telephone lines to a central computer installation.

Further improvement has been made in the methods used and the information furnished by these machines in both the area of receivables from customers and the area of merchandise records. We have increased the staff which is working on these problems. We expect electronic data processing to become increasingly important in our business in the years to come, and a vice-president of the Company is spending a major part of his time in these developments.

Long Term Debt

The total long term debt was reduced by a small amount during the year under review. A mortgage loan of $1,000,000 was placed against the new Joslin store property in Denver—which increased the debt. The regular payments of principal were made during the year totaling $1,241,072 ($583,000 on the insurance company loans and $658,072 on the mortgages). The result was a net reduction in total long term debt of $319,230, leaving the long term debt at $15,857,693 at January 31, 1966.

As to the Company's commitment under leases, there are currently 85 leases which extend more than 3 years. The minimum annual rentals under these leases aggregate approximately $2,407,724.

Working Capital and Short Term Bank Loans

The working capital continues to be entirely adequate for the current needs of the business. Working capital increased during the year by $2,508,175, and the total at January 31, 1966 was $42,075,189, (the first time this figure has been above $40,000,000). The ratio of current assets to current liabilities was 2.6 to 1 on January 31, 1966.

During the fall season we borrowed $2,000,000 from banks under short term notes. These loans were paid off before the end of our year. This is a smaller total than the comparable short term borrowings of recent years. For example, last year the figure was $4,000,000.

Return on Invested Capital

In the Financial Highlights shown in the front of this report, we have included figures for return on invested capital. There are several different ways of computing such a figure, and there seems to be no single generally accepted method. In our computation, we have related the net profit after taxes for the year—to the total of capital stock and surplus (net worth) at the end of the year (January 31, 1966).

Using the method just outlined, the return on invested capital was 12.8% for the year ended January 31, 1966 and the comparable figure for the preceding year was 11.3%.

Profit Sharing and Pension Plans

The funds in the Company's Profit Sharing Plan continued to grow during the year under review. The value of the Fund increased about 10% from investment gains (interest, dividends and changes in market values of securities). New record amounts were contributed into the Fund by our people and by the Company. The total dollar value of the Fund (at market value) increased from last year's total of $14,460,220 to the new total of $16,366,639. The latest total is summarized as follows:

Accumulated from contributions by our people.......	$10,044,034
Accumulated from Company contributions.......... (Invested in 158,594 shares of Mercantile Stores stock)	6,322,605
	$16,366,639

Our people contributed $1,308,277 of their own money into the Fund during the year (previous year $1,194,649). The Company contribution (geared to profits) amounted to $652,123 (a year ago the amount was $529,065). The contribution by the Company is deductible from taxable income.

As provided in the Plan, the Company contribution was allocated pro-rata among the people in the Plan in relationship to the amount each person contributed. The result was that each participant's account was credited with approximately 62 cents for each dollar contributed by the individual (up to 6% of salary). A year ago the comparable figure was 54 cents.

A large bank acts as Trustee of the Fund. The money contributed by our people is invested in various securities which are considered to be conservative investments. The money contributed by the Company is invested in one security only—Mercantile Stores stock. During the year under review, the Fund purchased 19,400 shares of Mercantile Stores stock. These purchases were made in the open market—with the purchases spaced out over twelve months.

There were 3,732 of our people in the Plan on February 1, 1966.

There is every indication that the Profit Sharing Plan is extremely popular among our people. They are very appreciative of what it does for them, and it is an important factor in building real loyalty to the Company.

The Company also maintains a Pension Plan which has been operating for twenty-one years. The funds in the Pension Plan amounted to $6,997,095 (at market value) on January 31, 1966. The Company pays the cost of the Pension Plan. Operations have been charged with $100,000 for the year under review—the same amount as last year. Securities in the Fund were sold during the last two years at prices well above the cost of such securities when purchased by the Fund. The profits realized on such sales resulted in keeping the cost to the Company at a lower figure. Two years ago, for example, the cost was $234,448. There were 2,758 of our people covered by the Pension Plan at January 31, 1966.

Current Trend

This report is being written in March. Business thus far in the new year (starting February 1st) has been good. General business throughout the country is at a high level and our own business reflects this. At March 15th the sales in our comparable stores are ahead of last year by about 9%. Whether or not these fine increases continue for the rest of the year, depends quite largely on how the general economy operates for the balance of the year.

Cash Flow

The cash flow for the year amounted to $11,956,000, equal to $4.06 per share. Last year the cash flow was $10,572,000, or $3.59 per share. There has been a steady increase in the cash flow over the past ten years, as shown in the chart below:

	Net Profit	Depreciation	Deferred Income Tax	Cash Flow
January 31, 1966	$8,600,000	$3,243,000	$113,000	$11,956,000
January 31, 1965	7,132,000	3,413,000	27,000	10,572,000
January 31, 1964	5,370,000	3,248,000	145,000	8,763,000
January 31, 1963	4,888,000	2,933,000	262,000	8,083,000
January 31, 1962	4,818,000	2,753,000	290,000	7,861,000
January 31, 1961	4,658,000	2,559,000	352,000	7,569,000
January 31, 1960	4,985,000	2,390,000	330,000	7,705,000
January 31, 1959	4,219,000	2,706,000	—	6,925,000
January 31, 1958	3,996,000	2,388,000	—	6,384,000
January 31, 1957	4,027,000	1,973,000	—	6,000,000

Source and Disposition of Funds

Funds were produced during the year from the following sources:

Net Profit	$ 8,600,344
Depreciation	3,243,417
New mortgage placed	1,000,000
Deferred income taxes	113,000
	$12,956,761

The summary below gives a quick picture of what use was made of these funds.

Disposition of funds during the
year ended January 31, 1966:

30%	($ 3,537,382)	paid out in dividends
38%	($ 4,560,238)	invested in capital assets
11%	($ 1,319,230)	used to pay off debt
21%	($ 2,508,175)	increase in working capital (Note A)
100%	$11,925,025	
	1,031,736	dividend declared in December, 1965 but not paid until March, 1966
	$12,956,761	Total Funds

Note A

The increase in working capital:

Cash up	$ 752,052
Receivables up	2,853,590
Inventory up	2,054,684
Current liabilities up	(3,121,093)
Miscellaneous	(31,058)
	$2,508,175

Some Comments About Our Merchandising Policies

We are giving more and more attention to fashion. In our opinion, our stores made real progress this past year in presenting, promoting and selling fashion. With our customers ready and able to spend money, real opportunities exist for selling more higher priced merchandise, and we are pointing our efforts in that direction.

In last year's report we commented on our two pronged policy of, on the one hand, selling large quantities of what is called private brand merchandise and at the same time actively promoting and selling nationally advertised brand goods. On this page are shown some of our more important private brands for which real acceptance has been built up over the years in our communities. Our experience of another year has again demonstrated that we can successfully sell both types of merchandise in our stores. In fact it gives the customer a greater assortment from which to choose. Customers generally like wide assortments.

Royal Heir

Infants' and small children's apparel and accessories.

Darcel

Women's Millinery Fashions.

Brookford CLOTHES

Men's suits, sport coats, and slacks.

Jean Sutton

Women's, misses', juniors', pre-teen, and girls' apparel and accessories.

Merville

America's first private brand for hosiery; also used in various fashion accessories, toiletries, and lingerie.

First Lady

Linens, domestics, draperies, home fashions, and accessories.

Royal Knight GOLD LABEL

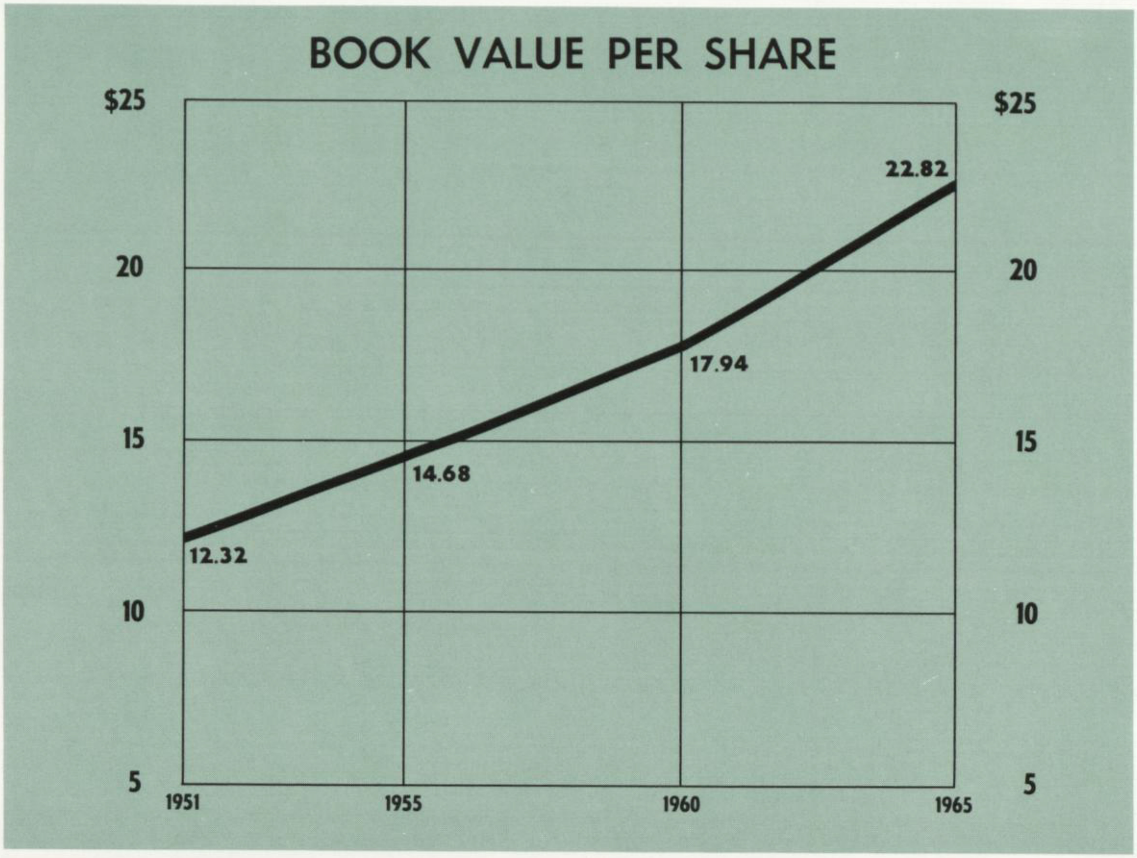
Men's and boys' furnishings, outerwear, and sportswear, and boys' clothing.

Various

Retained earnings (earned surplus) amounted to $55,705,205 at the end of the year, after an increase of $4,031,226 during the year.

The net worth (book value of common stock) of the Company was $67,254,620 at the end of the year. The book value per share has increased every year for over twenty-five years (after appropriately adjusting for stock splits). The book value at January 31, 1966 was $22.82 (a year ago $21.45). The Chart below shows the per-share figures over the last fifteen years.

The number of people regularly employed by the Company totals about 8,400. In peak periods the number approximates 12,000.



The financial statements, in comparative form, showing figures for the last two years, are given on the following pages, together with the report of our auditors, Arthur Andersen & Co., independent public accountants. Following that is a twenty-five year summary of the highlights of our business, together with a ten year comparison of balance sheets.

Our thanks go to the people in our Company whose cooperation is so important to a successful operation. We prize our good relationships with the concerns which sell us merchandise, and we thank them for working with us harmoniously.

Respectfully submitted,

Harold W Jorkers

Chairman of the Board

R. Nelson Shaw

President

ARTHUR ANDERSEN & CO.
NEW YORK, N. Y.

TO THE BOARD OF DIRECTORS AND STOCKHOLDERS,
MERCANTILE STORES COMPANY, INC.:

We have examined the consolidated balance sheet of Mercantile Stores Company, Inc. (a Delaware corporation) and subsidiary companies as of January 31, 1966, and the related statements of consolidated profit and loss, earnings retained for use in the business (earned surplus), and source and disposition of funds for the year then ended. Our examination was made in accordance with generally accepted auditing standards, and accordingly included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances. We had made a similar examination for the preceding year.

In our opinion, the accompanying consolidated balance sheet and statements of consolidated profit and loss, earnings retained for use in the business (earned surplus), and source and disposition of funds present fairly the financial position of Mercantile Stores Company, Inc. and subsidiary companies as of January 31, 1966, and the results of their operations and the source and disposition of funds for the year then ended, in conformity with generally accepted accounting principles applied on a basis consistent with that of the preceding year.

Arthur Andersen & Co.

New York, N. Y.,
March 31, 1966.

MERCANTILE STORES COMPANY, INC.

AND SUBSIDIARY COMPANIES

STATEMENTS OF CONSOLIDATED PROFIT AND LOSS
AND
EARNINGS RETAINED FOR USE IN THE BUSINESS (EARNED SURPLUS)

For the Years Ended January 31, 1966 and 1965

PROFIT AND LOSS

	Year Ended January 31,	
	1966	1965
Net sales, including sales of leased departments	$220,610,170	$207,260,905
Cost of goods sold, occupancy and central buying expenses, including depreciation and amortization of $3,243,417 and $3,413,289, respectively	156,345,566	147,902,837
Gross profit	$ 64,264,604	$ 59,358,068
Selling, operating and administrative expenses, less service charge income of $3,637,648 and $3,462,296, respectively	46,571,588	43,819,399
Operating profit	$ 17,693,016	$ 15,538,669
Other expenses (net):		
Interest expense	$ 1,619,001	$ 1,630,973
Less—Miscellaneous income (net)	516,329	344,539
	$ 1,102,672	$ 1,286,434
Profit before provision for income taxes	$ 16,590,344	$ 14,252,235
Provision for Income Taxes:		
Federal taxes	$ 7,280,000	$ 6,520,000
State and Canadian taxes	710,000	600,000
	$ 7,990,000	$ 7,120,000
Net profit for the year	$ 8,600,344	$ 7,132,235

EARNINGS RETAINED FOR USE IN THE BUSINESS (EARNED SURPLUS)

	Year Ended January 31,	
	1966	1965
Balance, beginning of year	$ 51,673,979	$ 48,079,126
Net profit for the year	8,600,344	7,132,235
	$ 60,274,323	$ 55,211,361
Dividends declared:		
$1.20 per share, paid in both years	$ 3,537,382	$ 3,537,382
$.35 per share paid in March 1966	1,031,736	—
	$ 4,569,118	$ 3,537,382
Balance, end of year	$ 55,705,205	$ 51,673,979

MERCANTILE STORES COMPANY, INC.

AND SUBSIDIARY COMPANIES

STATEMENTS OF CONSOLIDATED SOURCE AND DISPOSITION OF FUNDS

FOR THE YEARS ENDED JANUARY 31, 1966 AND 1965

	Year Ended January 31, 1966	Year Ended January 31, 1965
Sources of funds:		
Net profit for the year	$ 8,600,344	$ 7,132,235
Depreciation and amortization	3,243,417	3,413,289
Increase in deferred Federal income taxes	113,000	27,000
	$11,956,761	$10,572,524
Mortgage loan borrowing	1,000,000	—
	$12,956,761	$10,572,524
Disposition of funds:		
Dividends declared	$ 4,569,118	$ 3,537,382
Additions to property and equipment	4,560,238	3,770,776
Reduction in long-term debt	1,319,230	1,230,447
	$10,448,586	$ 8,538,605
Increase in working capital	$ 2,508,175	$ 2,033,919
Working capital at beginning of year	39,567,014	37,533,095
Working capital at end of year	$42,075,189	$39,567,014

MERCANTILE STO

AND SUBSIDIARY

CONSOLIDATED BALANCE SHEETS —

ASSETS

	January 31 1966	1965
Currents Assets:		
Cash	$ 9,558,155	$ 8,806,103
Accounts receivable—		
Customers accounts—		
Regular retail accounts	$ 8,769,411	$ 9,381,643
Installment accounts not sold	1,172,128	1,617,981
Equity in accounts sold (the uncollected balances of which amounted to $25,812,305 and $24,323,359, respectively)	15,764,826	12,064,180
Other accounts	982,907	728,454
	$ 26,689,272	$ 23,792,258
Less—Reserve for doubtful accounts	1,988,755	1,945,331
	$ 24,700,517	$ 21,846,927
Merchandise inventories, priced at the lower of cost or market	$ 32,178,978	$ 30,124,294
U. S. Government and other marketable securities, at cost, approximately equal to market	$ 1,746,778	$ 1,575,917
Unexpired insurance, prepaid rent, etc.	$ 652,209	$ 854,128
Total current assets	$ 68,836,637	$ 63,207,369
Property and Fixtures, at cost:		
Land	$ 8,007,667	$ 7,782,667
Buildings and building improvements	39,675,441	39,868,863
Less—Accumulated depreciation	(16,044,775)	(16,395,461)
Store fixtures, etc.	20,255,248	19,383,961
Less—Accumulated depreciation	(9,337,457)	(9,400,727)
	$ 42,556,124	$ 41,239,303
	$111,392,761	$104,446,672

RES COMPANY, INC.

COMPANIES

JANUARY 31, 1966 AND 1965

LIABILITIES

	January 31 1966	1965
Current Liabilities:		
Accounts payable	$ 11,939,491	$ 10,963,711
Dividends payable.	1,031,736	—
Accrued taxes (other than Federal income), compensation, rent, etc.	7,447,107	6,838,298
Reserve for Federal income taxes	5,034,509	4,607,899
Current maturities of long-term debt	1,308,605	1,230,447
Total current liabilities	$ 26,761,448	$ 23,640,355
Long-Term Debt:		
Notes payable to an insurance company—		
3⅜% notes, $250,000 due annually	$ 250,000	$ 500,000
5⅛% notes, $333,000 due annually to 1977, $2,500,000 due December 1, 1978	6,168,000	6,501,000
Mortgage notes payable, due in installments over the life of each mortgage, most of which are twenty-year mortgages	9,439,693	9,175,923
	$ 15,857,693	$ 16,176,923
Deferred Federal Income Taxes	$ 1,519,000	$ 1,406,000
Lease Obligations—see comments on page 18		
Capital Stock and Surplus:		
Common stock, par value $1.83⅓ per share—Authorized and issued 2,950,998 shares	$ 5,410,163	$ 5,410,163
Less—3,180 shares held in treasury	5,830	5,830
Outstanding 2,947,818 shares	$ 5,404,333	$ 5,404,333
Capital surplus	6,145,082	6,145,082
Earnings retained for use in the business (earned surplus)—$49,605,537 restricted at January 31, 1966, as to payment of cash dividends under terms of insurance company loan agreements	55,705,205	51,673,979
	$ 67,254,620	$ 63,223,394
	$111,392,761	$104,446,672

MERCANTILE STO

AND SUBSIDIARY

TWENTY-FIVE YEAR COMPARISON OF SALES,

Fiscal Year Ended January 31	Net Sales	Profit Before Income Taxes	Income Taxes	Net Profit	Net Profit Per Share (Note A)
1966	$220,610,170	$16,590,344	$7,990,000	$8,600,344	$2.92
1965	207,260,905	14,252,235	7,120,000	7,132,235	2.42
1964	192,408,732	11,160,157	5,790,000	5,370,157	1.82
1963	183,840,305	10,297,664	5,410,000	4,887,664	1.66
1962	175,820,970	10,068,178	5,250,000	4,818,178	1.63
1961	170,247,354	9,668,412	5,010,000	4,658,412	1.58
1960	167,799,529	10,375,430	5,390,000	4,985,430	1.69
1959	157,915,790	8,709,061	4,490,000	4,219,061	1.44
1958	153,994,341	8,177,638	4,182,000	3,995,638	1.37
1957	148,773,457	8,086,964	4,060,000	4,026,964	1.38
1956	138,785,704	8,036,717	4,120,000	3,916,717	1.35
1955	130,366,021	6,970,553	3,420,000	3,550,553	1.23
1954	130,882,985	6,933,491	3,410,000	3,523,491	1.22
1953	128,603,624	7,080,850	3,620,000	3,460,850	1.19
1952	124,699,947	6,442,260	3,322,000	3,120,260	1.05
1951	125,427,006	9,397,003	4,290,000	5,107,003	1.72
1950	112,607,776	5,932,129	2,325,000	3,607,129	1.21
1949	119,091,512	8,369,725	3,243,000	5,126,725	1.72
1948	113,012,702	8,444,538	3,286,000	5,158,538	1.73
1947	103,007,184	10,800,760	4,618,000	4,682,760	1.57
1946	74,407,149	5,894,901	4,084,000	1,810,901	.60
1945	59,668,304	6,633,941	4,854,000	1,779,941	.59
1944	50,277,807	4,700,875	3,276,760	1,424,115	.47
1943	41,173,113	3,340,264	2,118,645	1,221,619	.41
1942	34,867,853	1,912,941	812,165	1,100,776	.37

NOTE A:

In the above table wherever "Per Share" figures are given, such figures are all based on the stock after the 10 for 1 split in 1946 and the 2 for 1 split in 1962 and all prior year figures have been appropriately restated.

RES COMPANY, INC.

COMPANIES

EARNINGS AND RETAINED EARNINGS

DIVIDENDS PAID				
Common				
Per Share (Note A)	Amount	Preferred Amount	Retained Earnings (Earned Surplus)	Book Value Per Share (Note A)
$ 1.20	$3,537,382	——	$55,705,205	$22.82
1.20	3,537,382	——	51,673,979	21.45
1.00	2,947,818	——	48,079,126	20.23
1.00	2,947,818	——	45,656,787	19.41
.82½	2,431,950	——	43,716,941	18.75
.82½	2,431,950	——	41,330,713	17.94
.82½	2,423,777	——	39,104,251	17.18
.82½	2,415,029	——	36,542,598	16.35
.82½	2,411,835	——	34,738,566	15.74
.82½	2,402,442	——	31,654,763	15.22
.77½	2,248,742	——	30,030,241	14.68
.62½	1,809,999	——	28,362,266	14.12
.62½	1,809,999	——	26,621,712	13.52
.62½	1,836,849	$ 4,375	24,908,220	12.92
.50	1,470,404	17,500	22,915,344	12.32
.50	1,471,295	19,240	21,651,863	11.77
.50	1,481,220	22,040	18,035,395	10.03
.50	1,481,220	24,701	15,931,526	9.32
.50	1,481,220	25,676	12,310,722	8.10
.50	1,481,220	25,676	8,659,080	6.86
.12½	370,305	25,676	5,483,216	5.79
.12½	370,305	28,451	4,068,296	5.31
.12½	368,930	36,176	2,687,111	4.84
.12½	361,255	37,133	1,668,102	4.60
.10	290,444	40,187	844,871	4.29

MERCANTILE STO

AND SUBSIDIARY

TEN YEAR COMPARISON OF

	January 31,			
ASSETS	*1966*	*1965*	*1964*	*1963*
Cash and Marketable Securities	$ 11,304,933	$ 10,382,020	$ 10,139,787	$ 9,000,576
Receivables, less Reserve	24,700,517	21,846,927	20,556,089	27,225,565
Merchandise Inventories	32,178,978	30,124,294	29,665,608	28,926,550
Prepaid Expenses	652,209	854,128	885,806	723,221
TOTAL CURRENT ASSETS	$ 68,836,637	$ 63,207,369	$ 61,247,290	$ 65,875,912
Fixed Assets (Net)	42,556,124	41,239,303	40,881,816	39,765,753
	$111,392,761	$104,446,672	$102,129,106	$105,641,665

LIABILITIES				
Current Liabilities	$ 26,761,448	$ 23,640,355	$ 23,714,195	$ 28,585,153
Long-Term Debt	15,857,693	16,176,923	17,407,370	18,616,310
Deferred Federal Income Taxes	1,519,000	1,406,000	1,379,000	1,234,000
Capital Stock	5,404,333	5,404,333	5,404,333	5,404,333
Surplus Reserve	—	—	—	—
Surplus	61,850,287	57,819,061	54,224,208	51,801,869
	$111,392,761	$104,446,672	$102,129,106	$105,641,665
Net Working Capital	$ 42,075,189	$ 39,567,014	$ 37,533,095	$ 37,290,759

RES COMPANY, INC.

COMPANIES

CONDENSED BALANCE SHEETS

January 31,

1962	*1961*	*1960*	*1959*	*1958*	*1957*
$ 9,832,526	$ 8,374,386	$ 7,782,702	$ 8,517,822	$ 6,910,994	$ 7,048,251
15,778,321	15,120,028	14,741,032	12,985,902	12,491,754	13,302,895
27,070,761	26,087,816	27,429,533	24,562,675	24,511,645	24,794,615
914,171	1,171,057	1,057,629	1,029,165	1,238,460	990,185
$53,595,779	$50,753,287	$51,010,896	$47,095,564	$45,152,853	$46,135,946
38,020,878	36,873,849	36,837,080	36,651,716	33,562,828	29,794,822
$91,616,657	$87,627,136	$87,847,976	$83,747,280	$78,715,681	$75,930,768
$18,298,178	$16,214,399	$18,257,857	$21,019,367	$17,206,139	$17,652,613
17,080,123	17,850,609	18,606,453	14,828,883	15,447,820	13,892,909
972,000	682,000	330,000	—	—	—
5,404,333	5,404,333	5,404,333	5,369,591	5,363,872	5,347,188
—	—	—	—	—	1,500,000
49,862,023	47,475,795	45,249,333	42,529,439	40,697,850	37,538,058
$91,616,657	$87,627,136	$87,847,976	$83,747,280	$78,715,681	$75,930,768
$35,297,601	$34,538,888	$32,753,039	$26,076,197	$27,946,714	$28,483,333